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**INTERNAL AUDIT DIVISION  
OFFICE OF INTERNAL OVERSIGHT SERVICES**

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11 December 2001

To: Ms. Suzanne Bishopric, Treasurer  
Department of Management

From: Esther Stern, Director  
Internal Audit Division, OIOS

A handwritten signature in black ink, appearing to be "Esther Stern", is written over the "From:" line.

Subject: **OIOS Audit Number AF2001/34/1: Audit of the Iraq escrow account treasury and cash management functions**

1. I am pleased to present herewith our final report on the subject audit, which was conducted in July and August 2001.

2. Based on your response, we are pleased to inform you that we have closed Recommendations 6, 11 and 12 in the IAD recommendations database. We have also modified Recommendation 1. Recommendation 9 will be closed upon receipt of information concerning the integration of IMIS and OPICS. With regard to Recommendations 1 to 5, 7, 8, 10, and 13, we request that you reconsider your response based on the additional information we have provided in the report. Please provide a time schedule for implementing each accepted recommendation. I would appreciate receiving your comments by 10 January 2002.

3. IAD is assessing the overall quality of its audit process and kindly requests that you consult with your managers who dealt directly with the auditors and complete the attached client satisfaction survey form

4. I take this opportunity to thank you and your staff for the assistance and cooperation provided to the auditors in connection with this assignment.

Copy to:

Mr. J. Connor

Mr. B. Sevan

Mr. J.P. Halbwachs

UN Board of Auditors

Planning and compliance Officer, OIOS

Mr. D. Knutsen



**United Nations**  
**OFFICE OF INTERNAL OVERSIGHT SERVICES**  
**Internal Audit Division**



**Audit subject: Iraq Escrow Account Treasury and Cash Management Functions**

**Audit No. AF2001/34/1**

**Report date: 11 December 2001**

**Audit team:**

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**Audit of Iraq Escrow Account Treasury and Cash Management Functions**  
**AF2001/34/1**  
**Executive Summary**

In July and August 2001, OIOS conducted an audit of the Iraq escrow account treasury and cash management functions. The major objectives of the audit were to assess the adequacy of these escrow account functions; review the appropriateness of investment policy; evaluate bank reconciliation procedures; and assess the reliability of IT systems and controls.

**Results in brief:**

- ❑ The UN common principles and policies for investments (CPPI) had not been appropriately modified in order to meet the requirements of the Iraq Account and alternative policy guidelines had not been formulated.
- ❑ The CPPI limit the amounts that may be invested with a single institution based on its credit rating to: 5 per cent of total capital; and 10 per cent of the total portfolio. Escrow account investments have exceeded these guidelines by a wide margin, resulting in unacceptably high risks.
- ❑ Because the Banque Nationale de Paris (BNP) is the only bank authorized to issue humanitarian Letters of Credit (LCs) and since these LCs have to be fully collateralized, approximately 72 per cent of the escrow account is invested with BNP. There is a need to diversify both LCs and investments among a greater number of institutions in order to mitigate financial risks.
- ❑ The Treasury had taken steps to increase the number of institutions authorized to issue humanitarian LCs. However an insufficient number of banks were requested to make proposals, largely because the Government of Iraq (GOI) was reluctant to nominate additional institutions or to approve the institutions proposed by the Treasury.
- ❑ The Memorandum of Understanding (MOU) with Iraq stipulates that the GOI should be consulted when selecting banks for the escrow account. Despite this requirement, the Organization remains accountable for decisions and risks associated with limiting diversification of these funds.
- ❑ Investments have recently been made in callable certificates of deposit (CDs) with a maturity of up to three years. This investment strategy may result in a loss of capital should there be a need to liquidate the investment before maturity.
- ❑ Staffing levels in the Treasury's IT unit, LC operations and investment management were not sufficient to ensure the effective management of the account and provide adequate segregation of duties.

- ❑ The OPICS investment system used by Treasury has not been integrated with IMIS requiring the manual input of data, which could result in duplication of effort and increased risk of error.
- ❑ Responsibility for programming, maintaining and reconciling the OPICS system were not adequately segregated as the database administrator performed all of these activities. Furthermore, data input and authorization of data entered into OPICS were also not adequately segregated

Treasury did not agree that some of OIOS' findings, particularly those dealing with investment policies and decisions, posed any risk to the Iraq Account funds it manages. In general, Treasury was of the view that adequate controls were in place.

Major recommendations:

- ❑ Appropriate modifications should be made to the CPPI to address the areas where they are not applicable to the Iraq Account in order to provide guidelines for the large value of investments by the escrow account.
- ❑ In view of the large amount of funds in the escrow account and the Organization's legal responsibility for managing these funds, consideration should be given to establishing an investment committee to be responsible for developing investment policies. The committee could include a representative from the Central Bank of Iraq as provided for in the MOU with the GOI, to act in a consultative capacity.
- ❑ In order to prevent or mitigate the risks associated with having a higher than acceptable level of investments in only a few banks, a plan should be developed to further diversify the humanitarian LCs and investments among a larger number of institutions.
- ❑ Additional consideration should be given to investment maturity dates and types of financial instruments used, particularly with regard to the short-term nature of the programme, in order to prevent possible loss of funds due to early liquidation of investments.
- ❑ The Treasury and the Office of Programme Planning Budget and Accounts should assess how to integrate the OPICS system used by Treasury with the IMIS system in order to eliminate the manual input of data that may result in duplication of effort and errors.
- ❑ Steps should be taken to segregate duties with respect to programming, maintenance and reconciliation of the OPICS system, which are performed by the Treasury database administrator.

- ❑ Staffing requirements should be reassessed in order to strengthen management and segregation of duties in the Treasury's Escrow Account section.
- ❑ A specialized consultant should be engaged to review the appropriateness of the techniques used to manage the account and to strengthen financial risk management.

The Treasury did not in agree with some of the recommendations made including those calling for: alternative investment guidelines for the Iraq Account, a consultant to assess the investment policies and practices, and an investment committee to oversee Iraq Account investments.

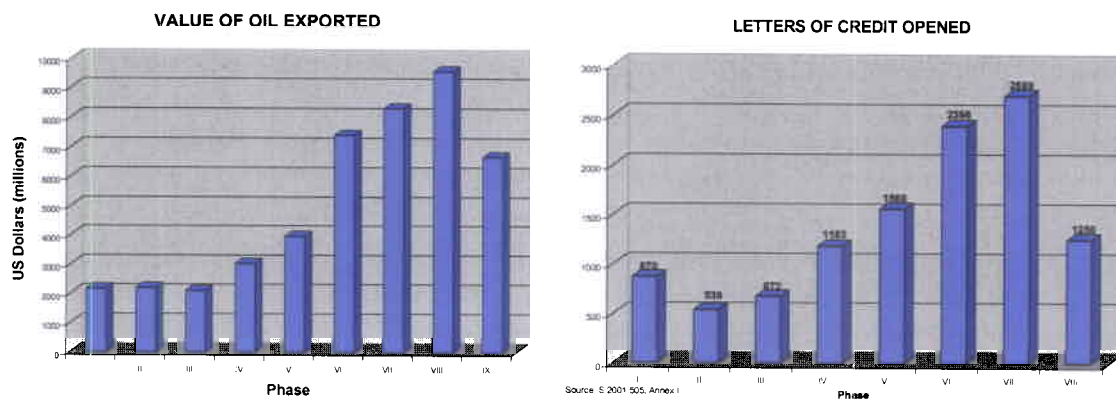
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## I. INTRODUCTION

1. In July and August 2001, OIOS conducted an audit of the Iraq escrow account. The audit was conducted in accordance with the general and specific standards for the professional practice of internal auditing in United Nations organizations. The Iraq escrow account was established by SCR 986 (1995) and a Memorandum of Understanding (MOU) signed by the Government of Iraq (GOI) and the UN for the deposit of revenues from the sale of oil authorized by the Security Council (SC). The escrow account is temporary in nature and does not constitute voluntary contributions by Iraq as a member state. Revenue is allocated to various accounts as established by SC resolution 986 (1995) of which 59 per cent is allocated for the purchase of humanitarian supplies by the GOI.
2. The UN Treasury's responsibilities include: (i) managing the investment of oil revenues; (ii) ensuring that oil revenues received are in accordance with contracts approved by the oil overseers, and (iii) arranging for the issuance of humanitarian Letters of Credit (LC) for goods purchased by the GOI under the distribution plan. Proceeds from the sale of oil are deposited into an account with Banque Nationale de Paris - Paribas (BNP). The UN Accounts Division is responsible for recording transactions in the UN accounts and for bank reconciliations. The Treasury has established a separate unit to deal with Iraq programme issues, which is staffed with four professional and seven general service staff. Three of the of the General Service posts are vacant
3. At the end of Phase IX of the Oil for Food Programme, 2.5 billion barrels of oil valued at \$44 billion had been exported by Iraq as shown in Figure 1 below. Figure 1 also shows that there has been a large increase in the number of humanitarian LCs processed by the Treasury.
4. The findings and recommendations contained in the report were discussed with management during the exit conference at which time a summary of the major findings was provided to them. Management's comments on the draft report are reflected in the report as appropriate and are identified in *italics*.

Figure 1



## **II. AUDIT OBJECTIVES**

5. The audit objectives were to: (i) assess the adequacy of the Treasury cash management function relating to the escrow account; (ii) review the appropriateness of investment policy and assess adequacy of internal controls; (iii) determine if United Nations financial regulations and rules have been complied with; (iv) review bank reconciliation procedures; (v) assess the reliability of IT reporting procedures and controls.

## **III. AUDIT SCOPE**

6. Based on the identified risks, the audit covered procedures for the receipt of oil revenues and disbursement of funds under the humanitarian LC arrangements. The audit also examined the investment policies for the escrow account, agreements with financial institutions and other documentation pertaining to the account. Although the audit covered all phases of the Oil for Food Programme, testing of transactions was limited to Phase IX. In addition, we interviewed officials of the Office of the Iraq Programme (OIP), Treasury, Accounts Division, and the oil overseers.

## **IV. FINDINGS AND RECOMMENDATIONS**

### **A. Escrow account administration**

#### Appropriate investment guidelines need to be established

7. The UN common principles and policies for investments (CPPI), approved in January 2000, state that conservatism and prudence rather than a speculative approach should be followed. The primary policies are:

- The investment horizon should not exceed 3 years maturity, and vary depending on the bank rating as follows: (i) less than or equal to 1 year for B/C rated bank; and (ii) less than or equal to 3 for years for AA rated banks.
- Amounts invested with any one bank are also limited according to the bank's ratings as determined by the Fitch International Bank Credit Analysis (IBCA) to: (i) \$150 million for A or A/B rated banks; (ii) \$90 million for B rated banks; and (iii) \$60 million for B/C rated banks. Also not more than 10 per cent of the portfolio should be held at any one institution, or the amount invested should be less than or equal to 5 per cent of the institution's capital/equity.
- Approved investments include: deposits, money market instruments, and fixed income marketable securities. Investment in equities is not permitted.

8. Our review indicated that escrow account investments had not complied with the CPPI. Although there was no specific documentation showing that these guidelines had been adopted for the escrow account, Treasury informed us that these guidelines did apply. Investment details and limits are shown in Figure 2 below. It is clear from these examples that further diversification is



required in order to provide an acceptable level of assurance that risks have been properly mitigated. In OIOS' view, there is a need to modify certain provisions of the CPPI so that they meet the requirements of the Iraq Account.

Figure 2

<b>Bank</b>	<b>IBCA Rating *</b>	<b>5% of Capital (\$ Million)</b>	<b>10 % of Portfolio (\$million)</b>	<b>Maximum Allowed (\$ Million)</b>	<b>Current Investment (\$ Million)</b>
Banco Bilbao Vizcaya Argentaria	B	942	128.1	90	1,078
Bayerische Hypo und Vereinsbank AG **	B/C	1,086	128.1	60	230
BNP – Paribas	B/C	605	128.1	60	3,368
Credit Agricole	B	1,358	128.1	90	350
Credit Suisse First Boston	B/C	389	128.1	60	0
Deutsche Bank	B	1,416	128.1	90	1,659

\* May 2001

\*\* Downgraded Jan. 2001. Fitch rating guide indicates negative outlook.

9. The Treasury's, Iraq Programme Unit makes decisions on investment maturity periods and transmits the information to the Senior Investment Officer, who determines the best available rates for this period and makes the investment. The Senior Investment Officer has discretionary authority to determine investment periods, types of investments and the institution where funds are to be invested. In OIOS' opinion, it would be more effective to establish an investment committee, responsible for various aspects of investing escrow account funds, such as establishing investment policies, determining appropriate types of investments and maturity periods, examining bank ratings, and reviewing and authorizing institutions in which funds can be invested. The feasibility of having the investment committee include representation from the Central Bank of Iraq in a consultative capacity, as provided for in the MOU with the GOI, should also be determined.

10. In view of the amount of funds which the Treasury is called upon to manage, the political sensitivity of investment decisions and use of the funds, and the high level of reputational risk to the Organization should any losses or other adverse factors affect the funds, we believe that specialized consultants possessing financial management risk mitigation expertise are required to review oil and humanitarian LC arrangements, investment policies and general management of the funds to ensure security of capital and any special requirements for the liquidation of the account should this become necessary.

### **Recommendations 1, 2 and 3**

OIOS recommends that the Treasury:

- (i) Make appropriate amendments to the CPPI to address areas

where the current regulations are not applicable to the Iraq Account (AF2001/34/1/01);

(ii) Establish an investment committee to oversee the investment of Iraq escrow account funds, comprising *inter alia*, representatives of OIP, Treasury, and the GOI, if deemed appropriate (AF2001/34/1/02), and

(iii) Engage a consultant with expertise in financial risk mitigation techniques to review the overall management of the Escrow Account in order to advise on appropriate procedures that need to be established to manage the account (AF2001/34/1/03).

11. *In response to the draft audit report, Treasury management advised that they did not agree with recommendations 01 to 03. Regarding recommendation 01, the Treasury stated that "the UN Common Principles and Policies on Investments (CPPI) apply to all investments placed by Treasury... including those for the UN Iraq Account..." However, the Treasury agreed that "the only noteworthy investment policy difference between the United Nations Iraq Account, ...and monies belonging to the United Nations outright is that the credit limits specified in the CPPI cannot apply to the United Nations Iraq Account."* Since this difference is the overriding feature of the CPPI, and because no alternative investment limits have been established, OIOS believes that there is a clear need to address this issue and establish appropriate limits. We were not informed of any authorization to exceed the CPPI investment limits. In our view, this is a serious shortcoming in the management of the Iraq Account and needs to be addressed urgently. We have modified this recommendation to clarify the required action, and therefore request that the Treasury provide us with the steps taken to amend the investment limits in order to make them more in line with the size of the Iraq Account investments.

12. *With regard to recommendation 02, the Treasury informed us that they "have an Investment Committee that meets twice annually and we see no reason to establish a second committee that deals exclusively with the UN Iraq Account since all investments placed by Treasury are processed using the same system (OPICS) and governed by the same policies (CPPI)." The Treasury did agree however, that in the future the Section Chief of the Treasury Oil-for-Food programme would attend meetings of the Committee.* However, we found that the current committee, made up of representatives from the UN, UNDP and UNJSPF, was formed to discuss overall UN investment policies and market conditions. It was not intended to specifically address Iraq Account investment matters, and was not designed to make investment decisions or to formulate policies. In view of the significance and special risks faced in managing the Iraq Account, the amount of funds involved, and the need to increase the perception of transparency, we reiterate Recommendation 2, and request that Treasury management reconsider its position on this issue and provide OIOS with a plan to establish an investment committee for the Iraq Account or alternative means to ensure the transparency of investment decisions.

13. *The Treasury did not believe there was a need to use an investment consultant to review current Iraq Account investment policies and procedures, as recommended in recommendation 03, since adequate expertise was available in-house.* However, in view of the magnitude of Iraqi funds under management and the political sensitivity involved, as evidenced by frequent inquiries from the GOI on this issue, we are of the opinion that an outside consultant should review the current investment and diversification policies. This would leave no doubt in the minds of interested parties that the Iraq Account is soundly managed and should therefore put to rest some of the criticism which the Treasury has endured. We therefore reiterate Recommendation 3, and request that the Treasury inform us of steps taken to implement it.

Further diversification of letter of credit arrangements is needed

14. Humanitarian LCs are entered into to pay for goods purchased by Iraq under the Oil for Food Programme. Under this programme, 59 per cent of oil revenues are allocated to the purchase of humanitarian supplies by Iraq. The purchase is subject to stringent conditions including Security Council approval of all contracts or by OIP in the case of "fast track" items, certification on arrival in Iraq by an independent customs inspector, and additional verification by Treasury and BNP before payment can be made. Our review of the payment procedure confirmed that the Treasury had established satisfactory internal controls to ensure the correct payment of contracts in a timely manner. These procedures satisfied the requirements of SCR 986 (1995) and the MOU with the Government of Iraq. Under the current arrangements, a contract has been entered into with BNP as the issuer of LCs. However, steps are being taken to diversify the issuance of LCs among other institutions.

15. Additional steps need to be taken to ensure additional security of collateral funds. On 24 July 2001, \$6.5 billion and €2.7 billion, representing approximately 72 per cent of escrow account funds, were deposited with BNP as collateral for humanitarian LCs and as invested funds. In our view, this represents an unacceptable risk and further diversification is needed to prevent possible loss of collateral funds. The Treasury is aware of the risks, and has, over several years, pointed out the need to diversify LCs among other banks. However, the GOI had not agreed to this change until recently. The Treasury has completed an exercise to increase the number of banks issuing LCs. The fee structure of the proposals received varied widely with the highest offer being approximately four times that of the lowest, which was from the current bank, BNP.

16. Requests for Proposals (RFPs) regarding the diversification of LCs have been sent to seven banks after consulting with the GOI, which had submitted a list of banks considered acceptable. However, in our opinion, a wider range of banks should have been invited to submit proposals in order to attain additional diversification since there is a continuing need to limit risks to a reasonable level. We also noted that broadening the number of banks that issue humanitarian LCs is important from an investment point of view since substantial collateral funds, which make up about 50 per cent of total funds, could only be invested with the institution that is issuing the LC. Furthermore, inviting additional banks to bid could have resulted in lower fees. It should also be noted, however, that diversification will result in additional work for the Treasury, which is currently operating at peak capacity. Therefore, staffing levels should be reviewed to determine any additional requirements.

## **Recommendations 4, 5 and 6**

OIOS recommends that the Treasury:

- (i) Establish a written policy for issuing humanitarian LCs and achieving diversification among banks, which identifies the basis for allocating LCs among the various banks, and the maximum value of LCs to be issued by individual banks (AF2001/34/1/04);
- (ii) Before finalizing the current LC diversification exercise, examine additional ways of diversifying LCs among a greater number of banks with acceptable credit ratings in order to reduce risks and to increase competitiveness that may result in lower LC fees (AF2001/34/1/05); and
- (iii) Determine if additional staffing is needed to handle the anticipated workload increase as a result of diversifying the issuance humanitarian LCs and investments (AF2001/34/1/06).

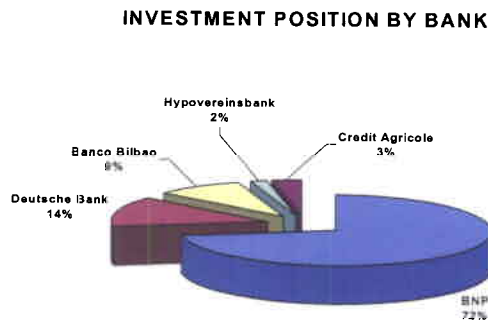
17. *In response to recommendations 04 and 05, the Treasury outlined some of the factors limiting the diversification of the Iraq Account. For example, for existing LCs, the buyer must either receive the goods or the LC must expire before diversification can be extended to other banks. We note that the Treasury has commenced a limited degree of diversification. However, in our view this effort has not been sufficient to achieve a desirable level of diversification. Furthermore, the Treasury has not established a policy to determine the basis for diversification and a plan to implement the policy. We therefore reiterate Recommendation 5 and request that the Treasury establish written policies with regard to diversification of LCs and develop a plan to further diversify the issue of new LCs among banks.*

18. *The Treasury agreed with recommendation 06 and stated that, with proper diversification of banking and LC arrangements there would be a need to at least triple the current staffing of the Treasury's oil-for-food unit and obtain additional IT staff. We have therefore closed this recommendation.*

### Investments need to be further diversified

19. Security, liquidity and return are the main criteria governing the investment of funds. In the case of the escrow account, security of funds should be the main criteria, since the funds are held in

Figure 3



Source: OPICS Investment & Security Position by Fund, 24 July 2001

The majority of investments are with BNP – Paribas resulting in higher than necessary risk to the funds. Some diversification has taken place, but the requirement to maintain collateral funds with BNP – Paribas has limited this effort.

trust on behalf of the GOI. While diversification through investing with banks other than BNP had been accomplished to some extent, the audit found that diversification had not been sufficient to adequately reduce the risk level. As shown in Figure 3, 72 per cent of funds, amounting to approximately \$3.4 billion, were still invested with BNP. Until diversification of LC issuance is completed, it will not be possible to reduce the investment held by BNP to a more realistic level. Additionally, all overnight funds are placed with BNP because of the limitations of the Global Payment System (GPS), a mailbox system, to facilitate multiple transfers in a speedy manner. Furthermore, all funds from maturing investments at other banks must be paid into BNP at maturity, further accentuating the risk.

20. Despite warnings from the Treasury since 1997 about the risks of not diversifying investments, the need to consult with the GOI and its reluctance to agree with the UN's proposals hampered the timely diversification of funds. The Treasury has also followed the policy of only investing in banks approved by the GOI, which has clearly limited the Treasury's options in this regard. However, the UN remains ultimately responsible for managing the funds in accordance with investment principles designed to limit risks. The fact that the GOI has not approved the proposed banks cannot be considered an acceptable rationale for not diversifying investments. It is therefore necessary for the Treasury to reach an additional understanding with the GOI on this matter and to advise them that UN investment policies apply to escrow account investments. However, consideration should be given to GOI requirements concerning matters such as determining the institution's country of origin in deciding where funds can be invested.

### **Recommendation 7**

OIOS recommends that the Treasury develop a plan to further diversify the escrow account investment portfolio by placing funds with institutions which have high credit ratings and that a list of these institutions be provided to the GOI for its review. In deciding how to diversify funds, primary consideration should be given to achieving

acceptable risk levels that comply with the established investment policies of the Organization (AF2001/34/1/07).

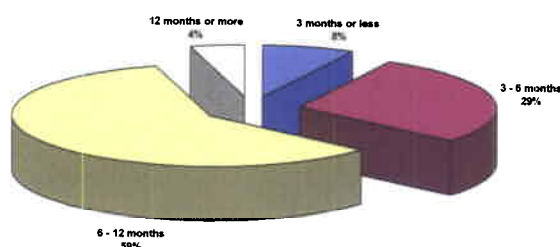
21. Regarding recommendation 07, the Treasury noted that it “categorically rejects OIOS’ suggestion that investments risks have not been properly mitigated. Treasury follows the rules of the CPPI to the letter.” However, as discussed in paragraph 8, we note that the Treasury has not adhered to investment limits as stated in the CPPI. While we understand the constraints faced by the Treasury, including the need to diversify LCs to other banks before investments can be fully diversified, and the need for consultation with the GOI, we stress the fact that the UN is solely responsible for managing the funds. It is therefore incumbent on the Treasury to develop a plan to achieve greater diversification within these constraints.

22. We therefore reiterate recommendation 7 and request that the Treasury provide OIOS with a plan to further diversify LC arrangements to other banks and a plan to further diversify investments of funds not collateralised.

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INVESTMENTS BY MATURITY

Figure 4



Source: Treasury summary for 25/07/01

Four per cent of investments have maturities of more than one year, while another 59 per cent have maturities from six to twelve months, which could affect the ability to quickly liquidate the account.

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#### Investment maturities need to be consistent with the Iraq Programme mandate period

23. Recently, some investments have been made in callable certificates of deposit (CDs) with maturity periods of three years. Figure 4 shows the maturity dates of the escrow account investments. While only 4 per cent of total funds are invested in callable CDs with maturity dates exceeding one year, this amounted to \$500 million. We understand that these maturity periods were selected based on the higher rates of return available, the availability of funds after determining cash flow requirements and the increasing level of funds available for investment. However, in view of the possible loss of principal, which may occur should the escrow account need to be liquidated on short notice, there is a need to review the implications of this investment strategy. Because of the escrow account’s short-term nature, liquidity should be a prime consideration when deciding on investments.



## **Recommendation 8**

OIOS recommends that the Treasury review the implications of its strategy to invest escrow account funds in callable CDs with maturities in excess of one year, considering the short-term nature of the Oil for Food Programme, and the risk of losing principal should an investment need to be liquidated before the maturity date (AF2001/34/1/08).

24. *In replying to recommendation 08, the Treasury informed us that they always take the programme mandate into account when making investment decisions and that the CPPI rules allow for terms of up to three years. They also noted that the CDs referred to in the report have been called and that the interest rate received was considerably higher than investments in fixed-term deposits of equivalent terms.* In our view, although the CPPI allows for investments of up to three years, this does not necessarily mean that this term is appropriate for Iraq Account investments. We maintain that investments should not exceed a realistic time period bearing in mind the nature of the programme and the need to retain liquidity should the programme end. This should also be one of the issues addressed by the investment committee, which we proposed in Recommendation 2. While we acknowledge the Treasury's comments, we maintain that investment terms should be commensurate with the programme mandate. We therefore re-iterate Recommendation 8, and request that further consideration be given to CD investment policies to ensure that investments with appropriate terms are made.

## **B. Transaction and data processing functions**

### Integration of the OPICS system and IMIS needs to be pursued

25. The critical systems used by the Treasury are the Operations Processing Integrated Control System (OPICS) and the Global Payment and Chase Insight Systems. Currently, the OPICS system is used to track investments, but the payments systems are not integrated with IMIS. Therefore, an OPICS report is generated monthly by the Treasury and submitted to the Accounts Division for manual input into IMIS.

26. Our review of data processing procedures found that entering data into IMIS manually results in a duplication of effort and is prone to errors, which could result in delays in the reconciliation and accounting processes. Data entry into IMIS is usually not current, and could adversely affect the investment functions and the timely issuance of accurate official reports on the status of the escrow account.

## **Recommendation 9**

OIOS recommends that the Treasury and the Office of Programme Planning, Budget and Accounts, jointly review costs, time frames, and other requirements necessary to integrate the IMIS

and OPICS systems in order to eliminate the manual entry of escrow account data, thereby increasing data entry accuracy and simplifying the reconciliation process (AF2001/34/1/09).

27. *The Treasury agreed with our recommendation that a daily interface should be established between OPICS and IMIS, but noted such limitations as a lack of resources within the IMIS project and concerns on the part of the Accounts Division. OIOS will close this recommendation when it receives additional information concerning joint efforts to integrate the IMIS and OPICS systems.*

Controls for processing investment transactions need to be improved

28. We reviewed the adequacy of the controls designed to verify the accuracy, completeness and authorization of investment transactions, carried out by the Treasury. The OPICS system uses a four-step security access system for processing transactions as follows:

- (i) Input/Approval
- (ii) Approval
- (iii) Release
- (iv) Send

However, we observed that the controls were not used effectively to ensure the accuracy of data input at an early stage. We identified several cases where the operator, who input the information from the Trade Blotters into OPICS also authorized the entry. That is, there was no segregation of duties between the input and authorization tasks.

29. These activities should be segregated to ensure accuracy and timely accounting and reconciliation. This is particularly important given the heavy reliance the Accounts Division places on the reports generated by OPICS, which are treated as the source documents for manual data entry into IMIS. We also found that although the operations manual addressed the technical aspects of OPICS, there were no documented IT policies and procedures outlining the existing controls.

**Recommendations 10 and 11**

OIOS recommends that the Treasury:

- (i) Establish and document well defined IT policies and procedures for the escrow account (AF2001/34/1/10); and
- (ii) Strengthen supervisory controls in the creation, approval and recording of escrow account investment transactions in OPICS to minimize operational risks and segregate functions relating to these activities (AF2001/34/1/11).

30. *Regarding recommendation 10, the Treasury believed that adequate documentation of the OPICS system was available. We were informed that the Database Administrator provides the*



*system support and that he relies on software user manuals and support provided by the vendor. We believe that in a complex system such as the OPICS, procedures to document the various aspects of the system, including data entry, reporting requirements, trouble-shooting, reconciliation and other internal control features are essential. This enables new users to familiarize themselves with the system and provides a basis for external users to assess the appropriateness of internal controls for the entry of data, reconciliation procedures and internal system control designed to ensure the integrity, accuracy and appropriateness of the data. None of these features had been documented for the OPICS system. We therefore reiterate this recommendation and request that the Treasury inform OIOS of relevant steps taken and the time frame for developing an operations manual.*

31. *The Treasury informed us that the Database Administrator is now enforcing "... the proper separation of duties by changing access rights of OPICS users to ensure that the same operator cannot input and approve the same transactions."* We have therefore closed recommendation 11 in our database.

#### Staffing support within the Treasury needs to be strengthened

32. Treasury IT staffing was limited to a single database administrator, which among other things, precluded the adequate segregation of duties. We observed that the database administrator is primarily responsible for programming, designing, maintaining and reconciling the OPICS and payment systems. His absence has resulted in lack of support and unwarranted down time. Moreover, consideration should be given to the impact of the proposed investment diversification, which will result increase the volume of transactions.

33. The database administrator, whose post is funded by the Iraq Oil for Food Programme, also spent over 25 per cent of his time on regular UN Treasury activities since the Treasury does not have other IT staff members. In OIOS' opinion, Treasury needs to review the adequacy of its current staffing of the IT Unit to identify any additional requirements.

34. It is also our view that the staffing requirement for processing oil and humanitarian LCs also needs to be reassessed. With the proposed diversification of both investments and LCs to a greater number of institutions, it appears that the current staffing level will not be able to meet the workload. With respect to responsibility for making investment decisions, two investment officers funded by the regular programme also have responsibility for the Escrow Account. In addition, decisions on investments time frames are also made by the Treasury's Escrow Unit, which does not provide for adequate segregation of duties. Considering the amount of funds involved and the scrutiny investment policies are subject to, it is our opinion that a dedicated post is required for this function. This will also improve segregation of duties between LC administration function and investment decisions, which in our view is critical.

#### **Recommendation 12**

OIOS recommends that the Treasury reassess staffing requirements of its IT, LC payment, and investment units in order to

strengthen internal controls, provide adequate segregation of duties, particularly with regard to the reconciliation process, and ensure that workflows are not interrupted particularly during the absence of the database administrator and other critical staff. (AF2001/34/1/12).

35. *The Treasury agreed with recommendation 12 and indicated that it is in the process of seeking approval for additional posts. We have therefore closed this recommendation.*

### **C. Other issues**

#### **Bank insurance requirements were not being monitored**

36. As stipulated in Article 1.15 of the respective bank agreements, each bank should “maintain insurance in an adequate amount to cover loss of or damage to funds or other property or assets held by it in connection with the performance of the agreement”. We made a comparative analysis of the insurance requirements specified in the bank agreements with the actual coverage and the actual portfolio held with each bank, which revealed that, although the amounts specified in the agreements were complied with, the amounts appeared inadequate given the size of the portfolios. Moreover, there was also no evidence of renewal of insurance policies and certificates on file, except for that of Credit Suisse, had expired. Treasury’s follow-up procedures appear to be lacking.

37. Treasury management informed us that the insurance clause in the bank agreements had originated at the beginning of the programme when it was anticipated that only minimal funds would be held in the escrow account. This was not the case, and it would not be feasible to insure the current large balances held in various institutions. Management also noted that bank ratings are the key industry indicator determining the security of funds deposited with an institution. In view of this, the Treasury should review the provision of the bank agreements and if the insurance requirement is no longer required amend the contract accordingly.

#### **Recommendation 13**

OIOS recommends that the Treasury review the insurance clause in the agreements with banks relating to the escrow account, and if it is determined that this requirement no longer exists amend the agreement accordingly (AF2001/34/1/13).

38. *The Treasury did not agree with recommendation 13 stating that “the clause exists because it is a standard in negotiations with other vendors.” They also informed us that “...leaving the requirements in the bank agreement allows the Purchasing Division to be consistent with all vendors.”* In our opinion, if this clause is an essential requirement of the agreement it is necessary for Treasury to follow up on the extension of insurance policies and establish a procedure to do this on a regular basis. OIOS therefore reiterates this recommendation and requests the Treasury to provide us with steps taken to implement appropriate procedures in this regard.

## V. ACKNOWLEDGEMENT

39. We wish to express our appreciation for the assistance and cooperation extended to the auditors by the Treasury, OIP and the Accounts Division.

A handwritten signature in black ink, appearing to be 'ES' followed by a stylized flourish.

Esther Stern, Director  
Internal Audit Division, OIOS